

## Internal Revenue Service

Number: **201033025**

Release Date: 8/20/2010

Index Numbers: 1001.00-00; 1223.00-00

Department of the Treasury

Washington, DC 20224

Third Party Communication: None

Date of Communication: Not Applicable

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PLR-151970-09

Date:

May 13, 2010

## LEGEND

Trust 1 =

Trust 2 =

Declarant =

Child 1 =

Child 2 =

Child 3 =

State Law =

Dear :

This responds to Trust 1's and Trust 2's requests dated November 18, 2009 for rulings about certain Federal income tax consequences of proposed transactions. You are the trustee of Trust 1 and Trust 2.

## FACTS

### Trust 1

Declarant formed Trust 1 in 1972 for the benefit of Declarant's children, grandchildren, and great-grandchildren. Declarant, Declarant's spouse, and three children (Child 1,

Child 2, and Child 3) have died. Child 1 and Child 2 each have three living children, and Child 3 has four living children. The ten living grandchildren are the current beneficiaries of Trust 1.

Article III(C)(1) of Trust 1 provides that the trustee shall pay or apply for the benefit of Declarant's children, grandchildren, and great-grandchildren such sums, from the income or principal of the trust estate, as the trustee in the exercise of its sole discretion deems advisable. Payments need not be equal.

Article III(C)(2) of Trust 1 provides that trust will terminate at any time that the trustee, in its absolute discretion deems it advisable to terminate such trust, provided, however, that in no event shall such trust terminate prior to December 31, 1981, and no later than twenty-one years after the death of all of Declarant's spouse, children, and grandchildren.

Article III(C)(3) of Trust 1 provides that upon termination all property and assets of the trust shall be distributed among Declarant's grandchildren, then living, in equal shares, and if any of Declarant's grandchildren is not then living, but leave children then living, such children shall receive the share that would have passed to their parent per stirpes.

The trustee proposes to exercise its authority to appoint the undistributed income and principal equally to ten new trusts, each for the benefit of one grandchild. Other than the beneficiaries, each new trust will contain the same provisions for the distribution of income and principal as are contained in Trust 1. Each new trust will contain a proportionate share of the assets of Trust 1 equal to the beneficial interest of each beneficiary in Trust 1's assets.

## Trust 2

Declarant and Declarant's spouse formed Trust 2 in 1971 for the benefit of Declarant's children, grandchildren and great-grandchildren. The ten living grandchildren are the current beneficiaries of Trust 2.

Article II of Trust 2 provides that the trustee shall pay all or part of the net income of Trust 2 to the beneficiaries. Article II of Trust 2 also provides that the amount of income distributed shall be determined in the sole and absolute discretion of the trustee. Payments need not be equal.

Article III of Trust 2 provides that the trustee may pay out to any individual income beneficiary an amount of principal as the trustee in its absolute discretion deems necessary for the care, support, education, illness or emergency of such individual income beneficiary.

Article IV of Trust 2 provides that trust will terminate at any time that the trustee, in its absolute discretion deems it advisable to terminate such trust, provided, however, that the trust shall terminate no later than the death of the last of Declarant's grandchildren. Article V of Trust 2 provides that upon termination of the trust all the principal and undistributed income of the trust shall be distributed per stirpes to the descendants of each of Declarant's three deceased children. Thus, each child of Child 1 and Child 2 would receive a pro rata distribution of one-ninth of Trust 2, while each child of Child 3 would receive a pro rata distribution of one-twelfth of Trust 2.

Article V of Trust 2 also provides that notwithstanding any other provision of the trust agreement, the trust shall terminate no later than 21 years after the death of the last of the survivor of the children, grandchildren, and great grandchildren of the trustors living at the time of the last of the trustors dies.

The trustee proposes to exercise its authority to appoint the undistributed income and principal to ten new trusts, each for the benefit of one grandchild. One-ninth of the principal and undistributed income would be distributed to the new trust created for the benefit of each child of Child 1 and Child 2, and one-twelfth of the principal and undistributed income would be distributed to the new trust for the benefit of each child of Child 3. Other than the beneficiaries, each new trust will contain the same provisions for the distribution of income and principal as are contained in Trust 2. Each new trust contains a proportionate share of the assets of Trust 2 equal to the beneficial interest of each beneficiary in Trust 2's assets.

## LAW AND ANALYSIS

Section 61(a)(3) of the Internal Revenue Code provides that gross income includes gain derived from dealings in property.

Section 1001(a) provides that the gain from the sale or other disposition of property is the excess of the amount realized over the adjusted basis provided in § 1011 for determining gain, and the loss is the excess of the adjusted basis provided in § 1011 for determining loss over the amount realized. Under § 1001(c), the entire amount of gain or loss must be recognized, except as otherwise provided.

Section 1.1001-1(a) of the Income Tax Regulations provides that, except as otherwise provided in subtitle A, the gain or loss realized from the exchange of property for cash or for other property differing materially either in kind or in extent is treated as income or loss sustained.

Rev. Rul. 56-437, 1956-2 C.B. 507, holds that the conversion of a joint tenancy in stock to a tenancy in common in order to eliminate the survivorship feature and the partition of a joint tenancy in stock are not sales or exchanges. Similarly, divisions of trusts are also not sales or exchanges of trust interests where each asset is divided pro rata

among the new trusts. See Rev. Rul. 69-486, 1969-2 C.B. 159 (pro rata distribution of trust assets not a sale or exchange).

State Law permits a trustee with discretionary authority under the terms of an irrevocable inter vivos trust agreement, to make a distribution of income or principal to or for the benefit of one or more beneficiaries of a trust to instead exercise such authority by appointing all or part of the income or principal subject to the power in favor of a trustee of a second trust subject to certain conditions and restrictions set forth in State statutes.

Here, Trust 1's assets will be distributed equally among the ten separate trusts. Each new trust contains a proportionate share of the assets of Trust 1 equal to the beneficial interest of each beneficiary in Trust 1's assets. Accordingly, the modification and severance of Trust 1 will not result in the realization of gain or loss under §§ 61 and 1001. In addition, because the modification and severance of the Trust 1 is not a taxable event under § 1001, the holding period of the assets that the ten separate trusts receive from Trust 1 will include the period that Trust 1 held those assets.

Trust 2's assets will be distributed pro rata to the descendants of Child 1, Child 2, and Child 3 among ten separate trusts. Each new trust contains a proportionate share of the assets of Trust 1 equal to the beneficial interest of each beneficiary in Trust 2's assets. Accordingly, the modification and severance of Trust 2 will not result in the realization of gain or loss under §§ 61 and 1001. In addition, because the modification and severance of the Trust 2 is not a taxable event under § 1001, the holding period of the assets that the ten separate trusts receive from Trust 2 will include the period that Trust 2 held those assets.

## CONCLUSIONS

Based on the information submitted and representations made we conclude that—

1. the modification and severance of Trust 1 will not result in the realization of gain or loss under §§ 61 and 1001 to Trust 1, the ten separate trusts, or their beneficiaries;
2. the holding period of the assets that the ten separate trusts receive from Trust 1 will include the period that Trust 1 held those assets;
3. the modification and severance of Trust 2 will not result in the realization of gain or loss under §§ 61 and 1001 to Trust 2, the ten separate trusts, or their beneficiaries; and
4. the holding period of the assets that the ten separate trusts receive from Trust 2 will include the period that Trust 2 held those assets.

We do not express or imply an opinion on the federal tax consequences of any aspect of these transactions other than those expressed in the conclusion above. For example, we express no opinions about the federal tax consequences of the

transactions under §§ 2601, 643, 661, 2036, 2037, 2038 and 2501, concerning which the Office of Associate Chief Counsel (Passthroughs & Special Industries) previously informed you that it had declined to rule.

This ruling is directed only to the taxpayer requesting it. Section 6110(k)(3) provides that it may not be used or cited as precedent.

The rulings contained in this letter are based upon information and representations that you submitted under penalties of perjury. While this office has not verified any of the material submitted in support of the request for rulings, it is subject to verification on examination.

Taxpayers must attach to any income tax return to which it is relevant a copy of this letter or, if they file their returns electronically, a statement providing the date and control number of this letter ruling.

In accordance with the Power of Attorney on file with this office, we are sending copies of this letter to your authorized representatives.

Sincerely,

Michael J. Montemurro  
Chief, Branch 4  
Office of Associate Chief Counsel  
(Income Tax and Accounting)